No. 8409.

# In the United States Circuit Court of Appeals

## For the Ninth Circuit.

12

J. N. Hendrickson,
*Complainant,*

*vs.*

El Camino Oil Company, Ltd., a Corporation,
*Respondent.*

State of California,
*Creditor and Appellant,*

*vs.*

H. A. Meek, as Receiver of El Camino Oil Company, Ltd., a Corporation,
*Receiver and Appellee,*

F. R. Kenney and L. W. Wickes,
*Creditors and Appellees.*



## BRIEF OF APPELLEE H. A. MEEK, AS RECEIVER OF EL CAMINO OIL COMPANY, LTD., A CORPORATION.

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## TOPICAL INDEX.

# INDEX TO AUTHORITIES CITED.

## Cases.



## Statutes.

TEXTS.

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## BRIEF OF APPELLEE, H. A. MEEK.

### I.

### STATEMENT OF THE CASE.

#### A. The Facts.

Appellee, H. A. Meek, is satisfied with appellant's statement of the case as to facts (App. Op. Br. pp. 4-8) with the exception following.

In appellant's statement of the case as to facts the statement is made to the effect that on June 6, 1930, the promissory note in the sum of $10,000.00 together with the mortgage securing the same was executed and delivered to appellees, F. R. Kenney and L. W. Wickes, and that on June 7, 1930, the promissory note in the sum of $80,000.00, together with deed of trust securing same, was executed and delivered to appellees, F. R. Kenney and L. W. Wickes (App. Op. Br. p. 5).

The stipulated statement of facts was as follows:

> ". . . that on or about June 7, 1930, said El Camino Oil Company, Ltd. made, executed and delivered two promissory notes in the amounts of Eighty Thousand ($80,000.00) Dollars and Ten Thousand ($10,000.00) Dollars, respectively, payable to F. R. Kenney and L. W. Wickes on demand and bearing interest at Seven (7%) Per Cent per annum compounded quarterly. That copies of said notes together with the instruments securing the same are attached hereto and made a part hereof." [Tr. p. 18.]

The copy of the trust deed [Tr. pp. 28-41] does not contain a copy of the $80,000.00 note, and apparently due to a mistaken impression that the said trust deed did contain a copy of said note a copy of the same is not set forth at any place in the transcript. However, a copy of the $80,000.00 note showing the same to bear the date of June 6, 1930 (the same date borne by the $10,000.00 note), is part of the claim filed by F. R. Kenney and L. W. Wickes, and the said $80,000.00 note is in fact dated June 6, 1930, and was executed at the same time as the chattel mortgage note in the sum of $10,000.00. While a copy of the $80,000.00 note does not appear in the tran-

script, neither does it appear by stipulation in the transcript that the $10,000.00 note bears an earlier date than the $80,000.00 note, nor that the $10,000.00 note was executed on a date prior to the $80,000.00 note, nor that the notes had different dates of maturity [Tr. pp. 18-19], all of which is assumed by the appellant to be disclosed by the transcript.

### B. The Questions Involved on This Appeal.

The appellee, H. A. Meek, is satisfied with appellant's statement of questions involved on this appeal.

## II.

## ARGUMENT.

### A. Answering Appellant's Point One.

### The Chattel Mortgage Executed by the El Camino Oil Company, Ltd. and Recorded June 10, 1930, in the Office of the County Recorder of Los Angeles County, Created a Valid and Existing Lien Securing the Claim of F. R. Kenney and L. W. Wickes.

Appellant's Point One (App. Op. Br. pp. 15-41) is to the effect that the chattel mortgage securing a note in the sum of $10,000.00 had been satisfied by an alleged credit, and therefore, the said mortgage is not an existing lien in favor of claimants and appellees, F. R. Kenney and L. W. Wickes. The alleged "credit" was the determination of the exact amount due F. R. Kenney and L. W. Wickes from the El Camino Oil Company, Ltd. in connection with certain "realization" contracts for the purchase of crude oil. [Tr. pp. 18-19.] Appellant cites and relies upon section 1479 of the California Civil Code.

The argument of the appellant assumes certain facts to be true that are not true and are not established by the evidence (Stipulated Statement of Facts), and the conclusions drawn by the appellant are erroneous in the following particulars:

1. Appellant assumes that the chattel mortgage and $10,000.00 note was executed and delivered June 6, 1930, and that the $80,000.00 note was executed and delivered June 7, 1930. As heretofore pointed out in this brief under "Statement of the Facts," both notes were dated June 6, 1930. Also the stipulated facts do not bear out appellant's assumption, the stipulation being that both notes were executed on or about the 7th day of June, 1930, and as part of the same transaction. At most the transcript does not disclose the exact date and terms of the $80,000.00 note, and it is contended that the Court cannot presume that the same was dated, executed or delivered subsequent to the $10,000.00 note.

2. Appellant contends that the $10,000.00 note and the $80,000.00 note were different or several obligations within the meaning of section 1479 of the California Civil Code, which provides:

> "Application of payments upon several obligations. —Where a debtor, under several obligations to another, does an act, by way of performance, in whole or in part, which is equally applicable to two or more of such obligations, such performance must be applied as follows:
>
> One. If, at the time of performance, the intention or desire of the debtor that such performance should be applied to the extinction of any particular obligation, be manifested to the creditor, it must be so applied.

Two. If no such application be then made, the creditor, within a reasonable time after such performance, may apply it toward the extinction of any obligation, performance of which was due to him from the debtor at the time of such performance; except that if similar obligations were due to him both individually and as a trustee, he must, unless otherwise directed by the debtor, apply the performance to the extinction of all such obligations in equal proportion; and an application once made by the creditor cannot be rescinded without the consent of (the) debtor.

Three. If neither party makes such application within the time prescribed herein, the performance must be applied to the extinction of obligations in the following order; and, if there be more than one obligation of a particular class, to the extinction of all in that class, ratably.

1. Of interest due at the time of the performance.
2. Of principal due at that time.
3. Of the obligation earliest in date of maturity.
4. Of an obligation not secured by a lien or collateral undertaking.
5. Of an obligation secured by a lien or collateral undertaking."

It is submitted that both notes and the instruments securing them were in fact one obligation given to secure a single indebtedness [Tr. pp. 18-19], the amount of which was undetermined at the time of the execution of the instruments, and such instruments cannot be held to be "several obligations" within the meaning of section 1479 of the Civil Code.

3. Appellant contends that the determination of the amount due was a credit on the obligation. A credit from F. R. Kenney and L. W. Wickes to the El Camino Oil Company, Ltd. assumes that the said F. R. Kenney and L. W. Wickes were indebted to the El Camino Oil Company, which was not a fact.

4. Appellant further assumes that the determination of the amount due was "an act by way of performance" on the part of the debtor as set forth in section 1479 of the Civil Code. It is submitted that an "act by way of performance" within the meaning of section 1479 is the rendition of services or the payment of money, and that the fact of determining the amount due was not an "act by way of performance."

5. Appellant further assumes that at the time of the alleged performance the intention or desire of the debtor was not carried out as provided in subdivision 1 of Civil Code section 1479. In that connection it is submitted that the intention of the parties, to the notes and instruments securing them, was that the properties described in both the trust deed and chattel mortgage should be pledged to secure the amount later determined to be due. Consequently, it was clearly the intention and desire of the debtor that the $10,000.00 note and mortgage securing the same should not be cancelled or satisfied upon the determination that the amount of the indebtedness was less than $80,000.00. This is further borne out by the fact that the note was not, in fact, cancelled.

6. Appellant further assumes that the creditors, F. R. Kenney and L. W. Wickes, did not make application of the alleged "performance" in accordance with subdivision 2 of Civil Code section 1479. It is submitted that

there is no fact that can be drawn from the stipulated statement of facts to support such conclusion.

7. Appellant further assumes that the notes were more than one obligation and further were obligations of different classes inasmuch as under subdivision 3 of Civil Code section 1479 it is provided that in the event there is more than one obligation of a particular class, a performance must be credited to all obligations in that particular class ratably. It is appellee's contention that the obligation or obligations as disclosed by the note are of a particular class in that they secure a certain same indebtedness and were executed as part of one transaction.

8. Appellant has erroneously concluded that subparagraph 3 of subdivision 3 of Civil Code section 1479 provides that if two notes are dated and executed on the 6th day of June, 1930, and the 7th day of June, 1930, respectively, and a part performance in connection with the said notes is made, then such performance shall be applied to the note executed at the earlier date. Such conclusion is not in accordance with Civil Code section 1479, subparagraph 3 of subdivision 3, inasmuch as the same provides that the performance shall be credited to the obligation *earliest in date of maturity*. Appellant has apparently assumed that the said Civil Code section provides that performance shall be credited to the obligation earliest in date of execution.

Appellant has further cited as authority for such conclusion the case of *McColgan v. Sockolov*, 192 Cal. 171. An examination of the facts in such case discloses that the obligations involved had various maturity dates, and the cited case is authority to the effect that the performance should be credited to the notes bearing the

earliest date of *maturity*. The fact that the notes bearing the earliest date of execution were the notes first maturing was incidental.

It must be assumed that the $10,000.00 note matured prior to the $80,000.00 note in order to give any consideration to appellant's contention. However, appellant did not contend that there was a difference in maturity dates, but only assumed a difference in execution dates.

It appears, therefore, that no error was committed by the District Court in holding the $10,000.00 note and chattel mortgage securing the same to be a valid and existing lien in favor of F. R. Kenney and L. W. Wickes on the property described in such chattel mortgage.

## B. Answering Appellant's Point Two.

### The Deed of Trust Executed by the El Camino Oil Company, Ltd. and Recorded June 10, 1930, in the Office of the County Recorder of Los Angeles County, Created a Valid and Existing Trust Securing the Claim of F. R. Kenney and L. W. Wickes.

The theory of the appellant under point two is to the effect that the trust deed included real property as Parcel 1 [Tr. p. 28] and personal property as Parcel 2 [Tr. pp. 29-30]. Then, assuming Parcel 2 to be personal property, appellant contends that the trust created as to the property described in said Parcel 2 is void as the instrument creating the trust was not executed as a chattel mortgage. Thus, appellant advances two contentions:

1. That the property described in Parcel 2 was personal property. The property under consideration as described in said Parcel 2 consists of:

(a) A leasehold interest in vacant land [Tr. pp. 48-57] plus an option to purchase the said vacant land [Tr. p. 53, paragraph 3];

(b) An oil refinery located upon Parcel 2, including all machinery, equipment and fixtures and all tanks, vats, pumps, boilers, engines, meters, pipes, stills and fractionating towers in whatever manner affixed or attached to said real property.

In considering the question of whether the property involved in Parcel 2 is real or personal, it is first important to determine the definitions of real and personal property as set forth in the Civil Code of the State of California. Title I of Part I relates to the nature of property, and section 657 provides:

> "Kinds of Property.—Property is either:
> 1. Real or immovable; or,
> 2. Personal or movable."

It is thus seen that personal property is movable property, and real property is immovable property. Further, in defining real property, we find that California Civil Code, section 658 provides as follows:

> "Real or Immovable.—Real or immovable property consists of:
> 1. Land;
> 2. That which is affixed to land;
> 3. That which is incidental or appurtenant to land;
> 4. That which is immovable by law; except that for the purposes of sale, emblements, industrial, growing crops and things attached to or forming part of the land, which are agreed to be severed

before sale or under the contract of sale, shall be treated as goods and be governed by the provisions of the title of this code regulating the sales of goods."

We thus see from section 658 that real property includes considerably more than land, and such fact is further borne out by the definition of land contained in California Civil Code, section 659, which provides:

"Land.—Land is the solid material of the earth, whatever may be the ingredients of which it is composed, whether soil, rock, or other substance."

Further, in construing section 658, wherein it provides that real property is that which is affixed to land, it is important to consider the provisions of California Civil Code, section 660, which provides:

"Fixtures.—A thing is deemed to be affixed to land when it is attached to it by roots, as in the case of trees, vines, or shrubs; or imbedded in it, as in the case of walls; or permanently resting upon it, as in the case of buildings; or permanently attached to what is thus permanent, as by means of cement, plaster, nails, bolts, or screws; except that for the purposes of sale, emblements, industrial, growing crops and things attached to or forming part of the land, which are agreed to be severed before sale or under the contract of sale, shall be treated as goods and be governed by the provisions of the title of this code, regulating the sales of goods."

In considering whether the property described in the deed of trust as Parcel 2 is real property or personal property, we will consider the same as heretofore divided under "A" and "B".

(a) As to the leasehold interest, it is to be noted that the courts of the State of California have not consistently held that a mere leasehold interest in land to be either real property or personal property. The appellant has cited certain authorities wherein a leasehold interest was held to be personal property, such cases being decided in 1904 and 1909. We wish to call the Court's attention to the case of *San Pedro, Los Angeles and Salt Lake Railroad Co. v. City of Los Angeles,* 180 Cal. 18, decided in 1919, wherein on page 21, it is held:

> "Section 3617 of the Political Code declares that the term 'property' includes 'all matters and things, real, personal, and mixed, capable of private ownership,' and that the term 'real estate' includes 'the possession of, claim to, ownership of, or right to the possession of land.' A leasehold estate carries a right to the possession of the land lease. (Civ. Code, sec. 819.) It is, therefore, real property within the above definition."

It is thus seen that the California Supreme Court in the cited case held a leasehold interest to be real property. Before proceeding to a consideration of the other property described in said Parcel 2, the Court's attention is called to the fact that the interest in the vacant land contained an option to purchase the said land in addition to the leasehold interest and thus was something more than a mere leasehold interest, and that the El Camino Oil Company, Ltd. had a further interest in the leased premises, that is, the ownership of the refinery improvements thereon which definitely determined the interest of said company to be real property as will hereinafter be pointed out.

Passing then from the consideration of the leasehold interest, we consider the other property described in Parcel 2:

(b) As to the refinery property, such property consisted of an oil refinery including all machinery, equipment and fixtures and all tanks, vats, pumps, boilers, engines, meters, pipes, stills and fractionating towers and was heavy machinery, tanks, pipes and buildings actually constructed on and attached to and part of the real property described in Parcel 2. A detailed description as to some of the said property is contained in the transcript, page 68-a. It is thus seen that the said property was actually affixed to land, and consequently, under the provisions of section 658 of the California Civil Code was real property. Such refinery property was owned by the El Camino Oil Company, Ltd. and was not leased from the owner of the land. (Although some of the property was being purchased on contracts and leases, if such property was not owned by the El Camino Oil Company, Ltd., the appellant herein could acquire no lien thereon as the act in question provides that the lien shall attach to the property of the distributor at the time of the distribution, and if at the time of the distribution, the property was not owned by the distributor necessarily no lien could attach under the terms of the act. The contract lien, of course, could apply to property, title to which was after acquired.)

The appellant seeks to overcome this definite conclusion that must be drawn from the facts, that is, that the said refinery property is real property by referring in its brief to the fact that in said trust deed it is stated that such property "shall be deemed to be real property" (App. Op. Br. p. 20), and that thus such property was recognized to

be personal property and must be so construed for the benefit of the appellant. By the same token it might be stated that such refinery property is real property since it is provided in the lease covering said land in paragraph 4 thereof [Tr. p. 54]:

> "(4) That boilers, engines, machinery, tanks, vats, stills, pipes, equipment and fixtures, and all personal property erected on said leased premises by the lessee may be removed by the lessee at the termination of this lease, or any extension thereof even though the same may be attached to said premises:"

and that inasmuch as by such provision the property is recognized as real property, it must be so construed to the detriment of the appellant.

It is submitted that the language contained in both the trust deed and the lease determines that the refinery property was treated as real property. However, it is conceded that such fact alone does not definitely determine the property to be real property.

An examination of the authorities cited by the appellant does not determine the interest of the El Camino Oil Company, Ltd. in the property described in the trust deed as Parcel 2 to be personal property. Considering briefly the authorities cited by the appellant, first is found the case of *J. S. Potts Drug Co. v. Benedict,* 156 Cal. 322, which holds that a mere leasehold interest is a chattel real and is personal property. There is no evidence that the owner of the leasehold interest owned any immovable or real property on the leased premises as in the present case. Also appellant cites the case of *Summerville v. Stockton Milling Co.,* 142 Cal. 529, wherein the facts are similar to the *Potts Drug Co. v. Benedict* case, and the

decision is the same. As heretofore pointed out, the authorities cited by the appellant are inconsistent with the case of *San Pedro, Los Angeles and Salt Lake Railroad Co. v. City of Los Angeles (supra)*, and that the courts of California are in conflict as to whether mere leasehold interests are real or personal property. However, the case of *Commercial Bank v. Pritchard,* 126 Cal. 600, *definitely determines that the interest of the El Camino Oil Company, Ltd. in and to the property described as Parcel 2 in the deed of trust is real property.*

In such case a lease of vacant land was made for a warehouse site for a term of five years with the option of either party to terminate the lease upon thirty days notice in writing and with the right to the lessee to remove the warehouse erected upon the leased ground at the termination of the lease and to renew the lease at the expiration of the term for a like period, the Court holding that such an interest was real property.

The interest of the lessee in the cited case was almost identical with the interest of the El Camino Oil Company, Ltd. in Parcel 2, and an examination of the lease relating to Parcel 2 [Tr. pp. 48-57], discloses that the lease was for ten years, gave authority for the erection by the lessee of a refinery [Tr. p. 52, paragraph 12], gave the lessee an option or right to purchase the leased land [Tr. p. 53, paragraph 3], gave the lessee the right to remove the refinery property erected on the premises [Tr. p. 54, paragraph 4], and gave the right of the lessee to renew the lease for a further term of five years upon its expiration [Tr. p. 53, paragraph 2].

Pursuant to such agreement the El Camino Oil Company, Ltd. erected upon such leased property a refinery. Some of the said refinery plant must be conceded to be

real property as being immovable and affixed to land. The case of *Commercial Bank of Santa Ana v. Pritchard (supra)*, definitely determines that since the improvements on the leased property were owned by the lessee and since such improvements were affixed to the real property, the improvements and the lease itself considered together were real property and were subject to a conveyance or encumbrance as real property by a deed or mortgage. It is, therefore, the contention of appellee that the cited case is definite authority that the interest of the El Camino Oil Company, Ltd. in and to said Parcel 2 is real property, and the Court is respectfully requested to read the complete decision in the case of *Commercial Bank of Santa Ana v. Pritchard*, 126 Cal. 600, as the same is considered decisive as to appellant's point two.

Further, under point 2, in addition to the contention advanced by the appellant that the property described in Parcel 2 was personal property as hereinbefore discussed, the second contention of the appellant is:

2. That the trust created as to said Parcel 2 is void as the instrument creating the trust was not executed as a chattel mortgage.

While appellee herein feels that the authorities hereinbefore cited definitely determine the interest of the El Camino Oil Company, Ltd. in Parcel 2 to be real property, nevertheless, it is likewise the contention of the appellee that the trust created as to Parcel 2 by virtue of the deed of trust is absolutely valid irrespective of whether the property therein described is real or personal property. Appellant's contention as to the invalidity of the trust is, of course, based upon the theory that the property described in the trust deed as Parcel 2 is personal property, and for the purpose of the argument, hereinafter it will

be assumed the property described in Parcel 2 to be personal property.

The Court's attention is directed to the fact that said deed of trust included Parcel 1 which is conceded by the appellant to be real property, and it is the appellee's contention that there can be created a valid trust affecting real and personal property under the terms of a trust deed as was used herein. Directing the Court's attention to the California law in relation to the creation of a trust, it is found that section 2220 of the Civil Code provides as follows:

> "Purposes for which trusts may exist.—A trust in relation to real and personal property, or either of them, may be created for any purpose or purposes for which a contract may be made."

Said section 2220 of the Civil Code was amended to read as above set forth in 1929. Prior thereto, the section provided as follows:

> "For what purpose a trust may be created.—A trust may be created for any purpose for which a contract may lawfully be made, except as otherwise prescribed by the titles on uses and trusts and on transfers."

Prior to such amendment of 1929, there was no specific provision in California law for the creation of an express trust as to personal property, that is, to the creation of a trust by agreement: there could, of course, be an implied trust created by law as to personal property, and, in fact, by decision, the California courts prior to 1929 recognized

the fact that a trust could be created as to personal property for any lawful purpose. However, the amendment of section 2220 in 1929 clarifies any question that there might be regarding the creation of such a trust, and, in fact, and by an examination of additional California code sections, it is seen that a so-called deed of trust can be a trust instrument as to personal property. For instance, an examination of section 725-a of the California Code of Civil Procedure discloses that the said section provides:

> "The beneficiary or the trustee named in a deed of trust upon real property *or any interest therein* to secure a debt or other obligation shall have the right to bring suit to foreclose the same, . . ." (Italics appellee's.)

In other words, the use of the words "or any interest therein", clearly discloses that a trust deed creating a trust can be effective upon any interest in real property, whether such interest is personal property or otherwise.

Furthermore, *a trust need not be created and acknowledged* as a chattel mortgage. In fact, the only provision as to how the same shall be created is set forth in section 852 of the California Civil Code, which provides:

> "Created by writing or by law.—No trust in relation to real property is valid unless created or declared
>
> 1. By a written instrument, subscribed by the trustee, or by his agent thereto authorized by writing;
>
> 2. By the instrument under which the trustee claims the estate affected; or,
>
> 3. By operation of law."

Certainly in the present case the trust agreement meets the requirements set forth in Civil Code, section 852. Furthermore, the authorities hold that no specific form is necessary to create a trust, the instrument need only express the intention of the parties. In fact, as heretofore pointed out, the only requirement relative to the execution of a trust is set forth in section 852 of the Civil Code, and the validity of a trust so executed is further recognized by section 2221 of the Civil Code, which provides:

> "Subject to the provisions of section eight hundred and fifty-two, a voluntary trust is created, as to the truster and beneficiary, by any words or acts of the truster, indicating with reasonable certainty:
>
> 1. An intention on the part of the truster to create a trust; and,
>
> 2. The subject, purpose, and beneficiary of the trust."

Further, a creation of a trust is not the creation of a lien. In fact, it is held "*in legal effect a deed of trust does not create a lien* or encumbrance upon the property, but conveys legal title to the trustee" (italics appellee's), *Weber v. McCleverty,* 149 Cal. 316, and it is further held that it is legally impossible for a trustee to have a lien on the property.

As heretofore pointed out, the argument in behalf of the State of California seems to be that since the property involved and described in the trust deed was to a great extent personal property, the trust created thereby

was void, and in connection therewith we wish to call the Court's attention to the case of *H. A. McDonald v. Smoke Creek Live Stock Co.,* 209 Cal. 231. In the cited case an instrument in the form of a deed of trust was executed covering both real and personal property, and thereafter the property was sold at a trustee's sale, and the action was one in which the purchasers and other claimants were litigating title to the property involved. The appellant contended that by virtue of the nature of the property, being both real and personal, the instrument was, therefore, one which was, in fact, an equitable mortgage requiring legal foreclosure. The Court sustained the judgment of the lower Court, holding that:

> "An instrument by which both real and personal property are conveyed to a trustee to secure payment of an indebtedness, which provides, upon default in the performance of its terms, for the sale of the property by the trustee, free and clear of any right of redemption, and also provides, in such event, for its foreclosure in a court of competent jurisdiction, is none the less a deed of trust, notwithstanding the dual nature of the remedies provided therein for its enforcement or the nature of the property conveyed, and such instrument is not required to be enforced by a suit in foreclosure, but the trustee may sell under its terms in case of default."

It is thus to be seen that a valid trust may be created involving real and personal property by a so-called trust deed. Further, it is contended that section 3440 of the

California Civil Code and section 2957 of the California Civil Code (such last section providing how chattel mortgages shall be executed) are not appliable to the present case for the following reasons: First, as heretofore pointed out, in 1929, section 2220 of the Civil Code was amended to specifically provide for the creation of a trust upon personal property. Second, the Civil Code sections relating as to how a trust shall be created do not require any particular form of execution or acknowledgment in connection with such creation of such trust. Such Civil Code sections specifically relate to the creation of a trust and consequently must be construed as not being affected by section 3440 of the Civil Code.

Section 3440 of the Civil Code is for the purpose of precluding fraudulent sales, and at the time the section was adopted, the California Legislature expressly contemplated the execution of chattel mortgages on personal property. At such time a trust as to personal property was not expressly contemplated by the Legislature, it being only in 1929 that the Legislature for the first time definitely contemplated trusts as to personal property. However, the specific provisions of section 2221 of the Civil Code, which provides in what manner a trust shall be created, determines the trust in the present case to be valid.

It is contended by the appellee herein as hereinbefore set forth that the deed of trust recorded June 10, 1930, created a valid trust in favor of F. R. Kenney and L. W. Wickes as to the property described in such deed of trust as Parcel 2 upon the ground that said property was real property, and further upon the ground that assuming the property in Parcel 2 to be personal property, the trust deed created a valid trust as to such personal property.

## C. Answering Appellant's Point Three.

### The Deed of Trust and Chattel Mortgage in Favor of F. R. Kenney and L. W. Wickes, Recorded June 10, 1930, Constitutes a Valid Lien Upon the Properties Described in Said Documents Prior and Paramount to Any Claim of the State of California as to Said Properties for Penalties Added to License Tax Due on Account of Motor Vehicle Fuel Sold and Delivered by the Camino Oil Company, Ltd. From and Including April 1, 1930, to and Including June 10, 1930.

Appellant's third point (App. Op. Br. pp. 26-31) is to the effect that penalties accruing August 15, 1930, upon the taxes due on account of motor fuel sold and delivered from the 1st day of April, 1930, to and including the 10th day of June, 1930, are a lien on the property of the El Camino Oil Company, Ltd., and became such a lien at the time of the distribution of the motor fuel, that is, prior to June 10, 1930.

The contention of appellant is predicated upon the theory that:

1. The act provides that the penalties shall be a lien on the property of the distributor, and in connection therewith it is important to consider the language of the act in question as it existed at the time of the distribution herein involved. Secton 4 of the California Motor Vehicle Fuel License Tax Act (California Statutes 1923, p. 572; Amended Statutes 1925, p. 659) in 1930 provided as follows:

> "Sec. 4. License taxes herein required to be paid shall be paid in quarterly installments to the state controller for the quarters ending December thirty-first, one thousand nine hundred twenty-three, and ending March thirty-first, June thirtieth, September

thirtieth and December thirty-first in the year one thousand nine hundred twenty-four and each year thereafter. *Said tax shall be a lien* upon all of the property of the distributor. It shall attach at the time of the delivery or distribution, subject to the tax, shall have the effect of an execution duly levied against all property of the distributor, and shall remain until the tax is paid or the property sold for the payment thereof. The amount of such license tax becoming due during each such quarter shall be paid within thirty-five days after the end of the quarter for which the same is due, and if not paid prior thereto shall become delinquent at five o'clock p. m. on the forty-fifth day after the end of such quarter, and ten per cent penalty shall be added thereto for delinquency." (Italics appellee's.)

It is to be noted from the foregoing that the act provides that the *tax* shall be a lien, but that the act is entirely silent as to any lien in connection with penalties therein provided for.

It is interesting to note that the legislature of the State of California amended the act in question, and in particular, section 4 thereof in 1931 so as to provide:

> "The controller shall seize any property, real or personal, used by said distributor in the operation of his business, and thereafter sell at public auction such property so seized, or a sufficient portion thereof, *to pay the tax due hereunder, together with any penalty or penalties imposed hereby for such delinquency,* and any and all costs that may have been incurred on account of such seizure and sale." (Italics appellee's.)
>
> *California Motor Vehicle Fuel License Tax Act,* Section 4 as amended by Statutes 1931, pp. 105, 1652, 2001 and 2288.

It is interesting to note that in amending the act in 1931 the legislature specifically provided that the property could be sold to satisfy in addition to the tax penalties imposed for delinquency. In fact, the language of the amendment provides first, *"to pay the tax due hereunder,"* and then further, *"together with any penalty or penalties,"* distinctly *recognizes that the tax and the penalties are not one.* If, as is the contention of the appellant herein, the tax and the penalties are one, why did the amendment in 1931 specifically provide for the sale to include a recovery for penalties? Why not stop when the legislature provided "to pay the tax due hereunder," if the penalties were properly included in such language as part of the tax?

2. The theory of the appellant, after assuming the act provides for a lien for penalties, further is to the effect that the lien for penalties relates back to the time of the distribution of the motor vehicle fuel, that is, prior to June 10, 1930, although it could not be determined until August 15, 1930, that any penalty would accrue. Appellant contends that a supposed lien (which is not provided for by the act) relates back to a time at which it could not be determined that any indebtedness could exist in order to support such lien, and in support of such position appellant cites two decisions of California courts, neither of which relates to penalties, and both of which relates to taxes directly imposed upon land for the benefit of the land.

It is conceded that on the first Monday of March in the state of California certain land taxes become a lien upon real property, the amount of which is to be later determined. It is definite and certain on the first Monday of March, when such lien becomes effective, that upon assess-

ment, the amount of such tax will be determined. In the instant case, it could not be definitely determined on and prior to April 10, 1930, that on August 15, 1930, or at any other time, certain penalties would exist. It also must be considered by the Court that the tax in question is not a direct tax upon the property involved or an assessment for improvements which confers a benefit on the land and enhances the security of the land and any encumbrances thereon, and it is submitted that an act imposing a tax of such character must be strictly construed as to any lien provisions.

Finally, in connection with appellant's Point Three, it is contended that it was within the discretion of the Court in this equity proceeding to disallow the appellant's claim for penalties, and that having such authority to disallow such penalties, the Court could properly determine in allowing the claim in what order the claim for the said penalties should rank in priority. It is conceded, of course, that an equity court need not follow the bankruptcy rule relating to penalties, but it is contended that it is discretionary with such equity court to do so.

*Medfield and Medway Street Railroad,* 215 Mass. 156, 163; 102 N. E. 415.

It is submitted that the District Court in determining the claim of the State of California for penalties in relation to the license tax on motor vehicle fuel sold and delivered prior to June 10, 1930, to be subject to the deed of trust and chattel mortgage in favor of F. R. Kenney and L. W. Wickes, recorded June 10, 1930, committed no error.

## D. Answering Appellant's Point Four.

### The Claim of F. R. Kenney and L. W. Wickes Constitutes a Lien Upon the Property Described in the Chattel Mortgage and Deed of Trust Prior to and Paramount to Any Lien of the Appellant Upon Said Property for License Taxes Due on Account of Motor Vehicle Fuel Sold and Delivered by the El Camino Oil Company, Ltd., Subsequent to the 10th Day of June, 1930.

The theory of appellant as to Point Four is to the effect that:

1. The legislature of the State of California has the power to make a tax lien paramount to an antecedent contract lien; and

2. That the California Motor Vehicle Fuel License Tax Act, section 4, as it existed in 1930, made the lien provided for in said section paramount to pre-existing contract litigation.

The appellee herein does not dispute the authority of the legislature to provide that upon a sale of property for a tax lien thereon, the purchaser shall acquire a title free and clear of contract liens, even though such contract liens were antecedent to the tax lien. However, it is the contention of appellee herein that section 4 of the said California Motor Vehicle Fuel License Tax Act did not make the lien provided for therein paramount to pre-existing contract liens.

The general rule as to rank of liens is provided in the California Civil Code:

"2897. First in Time—Bottomry Excepted.—Other things being equal, different liens upon the same property have priority according to the time of their creation, except in cases of bottomry and respondentia."

The Supreme Court of the State of California has from time to time considered the question as to whether tax liens are paramount to pre-existing contract liens, and there are two leading cases in the State of California on such subject. The first case decided in 1897 is *California Loan and Trust Co. v. Weis,* 118 Cal. 489. Said case interpreted various provisions of the California Political Code making the lien for personal property taxes a lien on the real property of the owners of such personal property. In such case it was held that the said tax lien was superior to pre-existing contract liens. The following quotations from such case clearly disclose the reasoning for the ruling of the Court in such case and establishes that the lien was expressly made by the Political Code paramount to antecedent contracts liens:

"It still remains to be considered, before leaving this branch of the case, whether the legislature of this state has, in the exercise of an unquestioned power, made the lien of its taxes paramount. As this matter, the power being conceded, depends for its determination entirely upon statutory enactment, adjudications in sister states will be of little value unless based upon identical laws.

"Our Political Code provides: 'Sec. 3717. Every tax due upon personal property is a lien upon the real property of the owner thereof from and after 12 o'clock M. of the first Monday of March in each year.' "

"'Sec. 3716. Every tax has the effect of a judgment against the person, and every lien created by this title has the force and effect of an execution duly levied against all property of the delinquent; the judgment is not satisfied nor the lien removed until the taxes are paid or the property sold for the payment thereof.'"

"After further provisions for the sale of the real property for all such delinquent taxes, it is provided:

"'Sec. 3788. *The deed conveys to the grantee the absolute title to the land described therein . . . free of all encumbrances, except the lien for taxes which may have attached subsequent to the sale.*'"

"No distinction is made by these laws between the lien which exists upon the land for the tax on personalty and the lien which exists for the tax upon the land itself. 'Every lien' created by this title remains until the taxes are paid or the property sold. *The title which the purchaser gets under the enforcement of any tax lien by sale is free from all encumbrances.*" (Italics appellee's.)

*California Loan and Trust Co. v. Weis,* 118 Cal. 489, at pp. 493-494.

It is important at this point to determine whether the act in the present case should be governed by the decision in the *California Loan and Trust Co. v. Weis* case, *supra,* and in considering the act in question, it is found that the same provides as follows:

"Sec. 4. License taxes herein required to be paid shall be paid in quarterly installments to the state controller for the quarters ending December thirty-first, one thousand nine hundred twenty-three, and ending March thirty-first, June thirtieth, September

thirtieth and December thirty-first in the year one thousand nine hundred twenty-four and each year thereafter. Said tax shall be a lien upon all of the property of the distributor. It shall attach at the time of the delivery or distribution, subject to the tax, shall have the effect of an execution duly levied against all property of the distributor, and shall remain until the tax is paid or the property sold for the payment thereof. The amount of such license tax becoming due during each such quarter shall be paid within thirty-five days after the end of the quarter for which the same is due, and if not paid prior thereto shall become delinquent at five o'clock p. m. on the forty-fifth day after the end of such quarter, and ten per cent penalty shall be added thereto for delinquency."

*Section 4 of the California Motor Vehicle Fuel License Tax Act (California Statutes 1923, page 572, Amended Statutes 1925, page 659) provided as above.*

A comparison of the Political Code sections set forth in the *Weis* case with section 4 of the California Motor Vehicle Fuel License Tax Act discloses that there is no provision in the license tax act providing that upon sale pursuant to such act title to the property sold should pass to the purchaser free of all encumbrances except liens for taxes. Thus the *California Loan Co. v. Weis* case is not decisive in the present matter.

Considering then the other leading California case decided in 1918, being the case of *Guinn v. McReynolds,* 177 Cal. 230, it is found that such case is an interpretation by the California Supreme Court as to the lien provided for in section 2322-a of the Political Code giving counties a lien for the expense of eradicating infectious

diseases and insect pests under the direction of the Horticultural Commissioner on private property. The Court states that such statutory lien bears an analogy to a tax or special assessment, and that a tax lien does not rank ahead of a pre-existing mortgage or other contract lien unless so provided by the act creating the lien. It is contended by the appellee herein that such case is decisive of the question herein involved, and that the quotations from such case as hereafter set forth clearly establish this contention.

> "The general rule for fixing the relative rank of liens is declared by section 2897 of the Civil Code, which declares that 'other things being equal, different liens upon the same property have priority according to the time of their creation, except in cases of bottomry and respondentia.' This rule will govern unless, in any given case, the statute prescribes otherwise."
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> *Guinn v. McReynolds,* 177 Cal. 230, at p. 232.

And further:

> "But the authorities declare, virtually without dissent, that even *a tax lien is not entitled to rank ahead of a pre-existing mortgage, or other contract lien, unless the legislative enactment creating the tax lien has given it priority.* (37 Cyc. 1143.) The priority need not be declared in express terms. It is enough if the intent to postpone contract liens appear by reasonable inference from the provisions of the act. But the authorization for displacing the earlier lien must, under all the decisions, be found in the statute." (Italics appellee's.)
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> *Guinn v. McReynolds,* 177 Cal. 230, at p. 232.

And further:

"In dealing with tax or assessment liens, as with others, our decisions have recognized that the question of priority is one of legislative intent. *Where,* accordingly, *the tax* or assessment lien *is preferred* to an earlier contract lien, *the basis of priority is found in the statute.* In *California Loan and Trust Co. v. Weis,* 118 Cal. 489 [50 Pac. 697], it was held that the lien for personal property taxes, imposed by our law upon the real property of the person assessed, was superior to pre-existing encumbrances upon the land. The question, said the court, 'depends for its determination entirely upon statutory enactment,' and the expression of a legislative intent that the tax lien should have priority was found in sections 3716 and 3788 of the Political Code, the former declaring that the lien is not removed until the taxes are paid, or the property sold, and *the latter that the tax deed conveys to the grantee the absolute title to the land, free of all encumbrances,* excepting liens for subsequent taxes. Similarly, in *German Savings and Loan Society v. Ramish,* 138 Cal. 120 [69 Pac. 89, 70 Pac. 1067], where the lien of street improvement bonds (Stats. 1893, p. 33) was held to have priority, it was pointed out that *the statute expressly provided that the lien should be 'a first lien upon the property,'* and that it made the provisions of the Political Code for the collection of delinquent state and county taxes, including section 3788, applicable to sales under the bond act. The opinion, after referring to these features of the statute, declares that 'the intention seems to be clearly manifested that the bond lien shall be prior to all liens.' In the decisions holding that the liens of assessments levied by irrigation districts or reclamation districts rank ahead of mort-

gages earlier in time (*Williams v. Cooper,* 124 Cal. 666 [57 Pac. 577]; *Weinreich v. Hensley,* 121 Cal. 647, 656 [54 Pac. 254]), there is no specific reference to any statutory declaration of such priority. But, on the examination of the acts involved, it will be seen that they plainly show the legislative intent. *The irrigation district law provides that the deed of the collector conveys to the grantee absolute title, free of all encumbrances,* except when the land is owned by the United States or this state. (Stats. 1887, p. 41.) The Political Code contains similar provisions with respect to reclamation districts. (Pol. Code, sec. 3466.)" (Italics appellee's.)

*Guinn v. McReynolds,* 177 Cal. 230, at pp. 232 and 233.

It is to be noted that in the decision of the Court in the *Guinn v. McReynolds* case the cases discussed therein where the tax lien was held prior to a pre-existing contract lien, some express language was found relative to the fact that upon a sale pursuant to such lien, title was passed free and clear of existing encumbrances, or that the lien was a first lien. The Court in said case further in considering section 2322-a of the Political Code states:

"*The section is silent on the subject of priority. The purpose of the expenditure for which the lien is given would not, of itself, justify a conclusion that the legislature must have intended to give it superiority over all other claims,* if, indeed, such inference can ever arise from the mere nature of the charge. *In the case of assessments for local improvements, it may be said that the improvement confers a benefit on the land itself, and thus enhances the security of the mortgagee.* But this is not necessarily true of expenditures made under the law here in question.

> The destruction of infected or diseased trees may diminish the value of the land, for the benefit, primarily, of adjoining property." (Italics appellee's.)
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> *Guinn v. McReynolds,* 177 Cal. 230, at pp. 233 and 234.

And in deciding the said case, the Court stated:

> ". . . we do not find in the act any provision indicating an intention to make the county lien superior to existing mortgages, and *it must be held,* as was held by the court below, *that the mortgagee is not affected by the subsequently attaching lien of the county."* (Italics appellee's.)
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> *Guinn v. McReynolds,* 177 Cal. 230, at p. 234.

It is submitted that the facts in the present case bear a close analogy to the facts in the case of *Guinn v. McReynolds, supra, for the following reasons:* The tax in the present case is not a tax on the property itself nor in the nature of an assessment for local improvements that might confer a benefit on the land and a benefit to the security of the liens. Further, the act under consideration does not contain any provision from which it can be concluded that upon a sale pursuant to the lien provided for by said act, such sale conveys to the purchaser title free from existing encumbrances.

Directing the Court's attention to the language of section 4 it is found that the only provisions contained in said section 4 relating to the effect of the lien to be as follows:

1. "Said tax shall be a lien upon all of the property of the distributor."
2. "It shall attach at the time of the delivery or distribution subject to the tax."

3. "shall have the effect of an execution duly levied against all property of the distributor" and
4. "shall remain until the tax is paid or the property sold for the payment thereof."

It is not contended by the appellant that the first three provisions above enumerated contribute any inference that the lien shall be prior to pre-existing contract liens. However, the appellant contends that the fourth provision above set forth gives the lien provided for in the act priority over pre-existing contract liens.

It is, therefore, important to consider such language, which is, "and shall remain until the tax is paid or the property sold for the payment thereof." The act prior to such language merely provided that the tax should be a lien, that the lien should attach at a certain time, and that it should have the effect of an execution duly levied. The execution that is therein referred to, of course, is the same as an execution issued pursuant to a judgment obtained in the usual procedure, and in considering what is the effect of an execution duly levied upon property, it is found that California Code of Civil Procedure provides in section 688 as follows:

> ". . . Until a levy, property is not affected by the execution; but no levy shall bind any property for a longer period than one year from the date of the issuance of the execution; provided, however, an alias execution may be issued on said judgment and levied on any property not exempt from execution."

It is thus seen that upon a levy of an execution the property is bound for only a period of one year. It is also said in California Jurisprudence as follows:

"Duration, Abandonment and Loss.—Under the law of California, the lien of a judgment continues for five years from the docketing of the judgment unless the enforcement of the judgment be stayed on appeal. When a judgment is a lien, the levy of an execution within that period neither creates any new lien nor extends the judgment lien. Consequently, in order for a judgment creditor to preserve the priority acquired by the lien of his judgment, he must cause a sale thereunder to be made during the statutory period of the lien.

"Abandonment and loss.—If personal property which has been levied upon under an execution is abandoned to the control of the debtor, the lien of the execution ceases to exist as against subsequent lienors. Under such circumstances the levy cannot operate to defeat a subsequent execution, and an existing mortgage lien immediately acquires priority against it."

11 *Cal. Juris.* 72, Executions, Sec. 27.

Referring again to the act in question and to section 4 thereof, it is found that if it were not for the provision that the execution should remain until the tax is paid or the property sold for payment thereof, the execution would cease to bind the property upon the lapse of one year from the date of distribution (the time the execution is deemed to be levied).

The statement that the execution lien shall remain until the tax is paid merely does away with the one year limitation as provided for in section 688 of the Code of Civil Procedure and also the further code provision to the effect that an execution on a judgment is to be issued within five years from the date of the judgment which

is provided for by California Code of Civil Procedure, section 681. The provision contained in section 4 of the act that the execution lien shall remain until the property is sold for the payment thereof certainly does not infer that upon such sale title free and clear of all encumbrances shall pass to the purchaser. In fact, a sale pursuant to an execution procured in the usual manner could well be said to remain a lien upon the property executed upon until the judgment (tax) is paid, or the property executed upon sold for the payment thereof (or one year has elapsed as provided for by C. C. P. 688).

It is submitted to the Court that the only additional effect added to execution by the language of section 4 of the act in question is to do away with the possibility of any lien claimed thereby expiring by lapse of time, and that such act does not provide that upon the sale of property pursuant to the lien granted in such act title shall be passed to the purchaser free and clear, or that the lien is a first lien.

As an illustration to the Court, let us assume that John Doe, an individual, was engaged in the distributing of gasoline and that he owned a home of the value of $5,000.00, which was homesteaded, and that on June 10, 1930, he was indebted to the State of California for taxes pursuant to section 4 of the act in question. Such act provides that the tax shall be a lien on all property of the distributor which would include, of course, his home. Let us further assume that the State attempted to make a sale of the home to satisfy its lien. Of course, under an ordinary execution the property would be exempt by virtue of being homesteaded. However, if the act in question provided that upon a sale pursuant to the lien provided for, the purchaser should acquire a clear

title, or a clear title except for subsequent tax liens, the homestead would not save the property for the debtor. Certainly the Court cannot so construe the language contained in such act.

It is submitted, therefore, that the District Court properly held that the lien of F. R. Kenney and L. W. Wickes provided for by the said chattel mortgage and trust deed was prior to any lien of the State of California as to motor fuel distributed after June 10, 1930, and that the decision of the District Court set forth in the transcript ["Memorandum of Decision," Tr. p. 75, at pp. 77-81], was correct, and this Court's attention is respectfully directed to such decision.

## III.

## CONCLUSION.

In concluding, it is submitted that no error was committed by the District Court, and that the decision must be affirmed in all respects.

The District Court in this matter was sitting as a court of equity, and no contention has ever been made that the claim of F. R. Kenney and L. W. Wickes was not a valid claim based upon a legal indebtedness, and that there was adequate consideration to support such claim and the lien claimed in connection therewith.

Respectfully submitted,

EARL GLEN WHITEHEAD,

*Attorney for H. A. Meek as Receiver of the El Camino Oil Company, Ltd., a Corporation, Receiver and Appellee.*